



STATE OF CALIFORNIA

STATE BOARD OF EQUALIZATION

450 N STREET, SACRAMENTO, CALIFORNIA
PO BOX 942879, SACRAMENTO, CALIFORNIA 94279-0082
TELEPHONE (916) 324-2655
FAX (916) 323-3387
www.boe.ca.gov

JOHAN KLEHS
First District, Hayward

DEAN ANDAL
Second District, Stockton

CLAUDE PARRISH
Third District, Torrance

JOHN CHIANG
Fourth District, Los Angeles

KATHLEEN CONNELL
State Controller, ~~Sacramento~~

JAMES E. SPEED
Executive Director

October 11, 2000

Dear Mr. _____ :

On November 12, 1999, we replied to your request for our evaluation of the change in ownership and reassessment consequences of a possible merger of a lease into a fee. Since that time, you have learned that the facts are not precisely as you understood and stated them in your original request. As such, you restate your request setting forth the corrected facts you have subsequently discovered, and again request our opinion whether the proposed termination of the Lease would result in a change in ownership. We conclude that the same analysis as is set forth in our November 12 letter is also applicable to the facts you now present.

Our November 12 opinion was based upon the following facts. The Lease in question impacts a shopping center, and was executed by the then owner in 1972 granting a total lease term, including renewals and options, of 90 years to one of the owner's wholly-owned subsidiaries, as tenant. The remaining term of the Lease is now 63 years. The present owner, A, acquired the fee in 1978, and a subsidiary of the owner, X, received an assignment of the tenant's interest in the Lease, at the same time, from the original tenant. The present owner, A, is desirous of "cleaning up" the title to the property and desires to eliminate the Lease, providing that this does not result in a reassessment of the property. You advised us that the present owner, A, and the present tenant, X, are still an affiliated group, which we assumed means that the tenant is a wholly-owned subsidiary of the owner.

We concluded that, under the situation you described, terminating the Lease, thereby effectively transferring the leasehold interest back to the present owner, A, would not constitute a change in ownership, or require a reassessment of the property, because it would be a transfer of real property among members of an affiliated group under the change in ownership exclusion of subdivision (b) of Revenue and Taxation Code section 64 and Property Tax Rule 462.180.

You have learned, however, that the tenant's interest in the Lease was not "assigned" to the subsidiary of the present owner, X, at the time the fee was acquired but rather, the property was subleased to it. The original tenant under the Lease was merged into the parent corporation of the original landlord (which, of course, was also the parent of the original tenant) a few days before the 1978 transfer of the fee occurred. The parent, which then became the tenant by means of the merger, then subleased the property by what is commonly known as a "pass through" sublease, to the subsidiary of the present owner, X. The sublease expires one day prior to the expiration of the Lease, and provides, among other things, that the subtenant, X, has the right to terminate the Lease.

A "pass-through" sublease is, in effect, an assignment of all of the rights and obligations of the lessee/sub-lessor in the property to the sublessee. Since many leases have prohibitions against assignment, and since lenders often prohibit assignment when improvements are security for loans, "pass-through" subleases are used to avoid violating such prohibitions. Though written as a sublease, all the rights and interests of the former lessee "pass through" to the new sublessee, with the result that the former lessee has nothing left except for one minimal right or interest, the right to hold the property one day longer than the sublessee, which distinguishes a sublease from outright assignment. Since the former lessee has, in effect, transferred the full value of its leasehold estate, the transfer is, *in substance*, an assignment, though, *in form*, it reads like a sublease. This situation is an exception to the general rule that a landlord may not collect rent from a subtenant. (See Civil Code sections 1995, et seq.)

Thus, the parent corporation of the original landlord remained a "sublessor" under the 1978 "pass through" sublease to the present tenant, X, in name only, as the full beneficial interest in the property transferred at that time. As the result, the present tenant's, X's, rental obligation was to the present owner, its parent, A.

Under these facts, both the Lease and the sublease have an original and remaining term of 35 years or more. The termination of the Lease and sublease, effectively transferring the Lease to present owner, A, would therefore be a change in ownership pursuant to subdivision (c)(1) of Revenue and Taxation Code section 61, absent an applicable exclusion. However, as in the previous fact pattern, here the transfer would be from a one hundred percent-owned subsidiary, X, to its parent corporation, A. As such, it again would fall within the exclusion for transfers of real property among members of an affiliated group set forth in section 64(b) and Rule 462.180. Therefore, it continues to be our opinion that the transfer of the Lease from the subsidiary to the parent corporation would be properly excluded from change in ownership and reassessment, even with the amended facts submitted subsequent to our earlier opinion.

October 11, 2000

Page 3

The views expressed in this letter are advisory only; they represent the analysis of the legal staff of the Board based on present law and the facts set forth herein, and are not binding on any person or public entity. You may wish to contact the Los Angeles County Assessor's Office to ascertain whether the assessor agrees with the above-mentioned views/analysis.

Sincerely,

/s/ Daniel G. Nauman

Daniel G. Nauman
Senior Tax Counsel

DGN:tr

prop/prec/13leases/00/03dgn

cc:

Mr. Dick Johnson, MIC:63
Mr. David Gau, MIC:64
Mr. Charles Knudsen, MIC:62
Ms. Jennifer Willis, MIC:70